NATIONAL BANKING AND THE CLEARING-HOUSE.

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THE national banking law, at the time of its enactment, was essentially a transcript from the laws of New York and Massachusetts, with changes necessary to nationalize their provisions, together with some distinctively new features. The system was established at a time of great financial pressure (1863) to supply the monetary needs of the government, State banks having proven inadequate. United States bonds, exclusively, were made the basis for circulating notes, and thus the banks became large purchasers of bonds, and note-holders were protected beyond possibility of loss. Many important amendments have since been made, all of a restrictive character.

The affirmative action of banks, within the line of statute and common law, is left to their individual enterprise, inspired by the desire of stockholders for dividends. The function of the government is to regulate by restraining. It seeks to insure good banking by enforcing statutory prohibition against unsafe practices.

Five or more persons may organize a national bank, and receive their charter from the Comptroller of the Currency. Banks may be organized with a minimum capital of fifty thousand dollars in places of less than six thousand inhabitants, one hundred thousand dollars where the population does not exceed fifty thousand, and with two hundred thousand capital in all larger places. Banks must own United States bonds equal to one-fourth of their capital stock, if the capital does not exceed one hundred and fifty thousand, and in case it does must own not less than fifty thousand dollars of such bonds. Any national bank may acquire and assign to the United States Treasurer, bonds of the United States not

exceeding the amount of capital stock, upon which security the Comptroller issues circulating notes equal to ninety per cent. of the par of such bonds. In 1863 Congress imposed a ten per cent. tax on State-bank circulation, which was intended to and did force it out of existence.

Banks make five verified reports of condition annually, in such form as the Comptroller prescribes, upon a post-dated notice, which reports are compiled and reported to Congress, and the balance sheets published in the local press. These reports are elaborate as to balance sheet and detail, and since the books of each bank must be so kept as to furnish this information, it has an important and valuable influence in systematizing bookkeeping and unifying methods of business. The compilation of these reports reflects the course of trade and finance throughout the country, and is of great practical value to the public.

Each bank is examined at least once a year by an expert examiner, appointed by the Comptroller of the Currency and Secretary of the Treasury. The scope of examination includes compliance with the law, character and method of business, fitness of officers, valuation of assets, and ascertainment of liabilities.

National banks are restricted to a commercial banking business, cannot loan upon real estate security, and real estate holdings are limited to banking necessities and property acquired to protect the bank against loss; cannot loan upon or own their stock; are forbidden to borrow money to an amount exceeding paid-up capital; are forbidden to certify checks, except against money actually on deposit, and are forbidden to loan to any one individual, corporation or firm an amount exceeding ten per cent. of their capital.

Causes affecting a whole community, like general financial distress, repeated crop failures in one locality, may cause bank failures, but the history of bank failures and large losses, which do not result in failure, reveals as a common cause the concentration of the bank's funds in a few hands or a few interests. This prohibition seeks to distribute a bank's loans and thus reduce its risks. New York, Chicago and St. Louis are central reserve cities, and banks located therein are required to keep, in bank, a cash reserve equal to twenty-five per cent. of their net deposits. There are twenty other reserve cities, the banks in which are also required to keep a like reserve of twenty-five per cent., one-half of

which must be cash in bank and the remainder may be to their credit with a central reserve city bank, approved by the Comptroller. Banks located elsewhere are required to keep a like reserve of fifteen per cent., six per cent. of which must be in cash in bank and the balance may be with an approved bank in any reserve city. This requirement does not seek to establish a new principle in banking. Its purpose is to compel all banks to keep such reserve as conservative banks would keep in the absence of any regulation.

The percentages required are based upon the experience of conservative banks, conform to the requirements of prudence, and are designed to be so fixed that in the regular course of business a bank would as often be over as under its reserve. The reserve is not a fixed quantity, segregated from the current funds of the bank. It is there to be used when required. The statute contemplates such use, but requires its restoration in due course of business. And if, after notice from the Comptroller, it fails for thirty days to make its reserve good, the bank may be closed.

An interior bank cannot safely transact its current business with less than six per cent. of its deposits in cash on hand. And reserve city banks, with their liability to be drawn upon, "in flocks," by their correspondents, require the increased amount. Stockholders are liable to an assessment to make good an impairment of capital, and, in case of failure, are liable to assessment to an amount equal to the par of their holdings, in order to pay creditors. In case of failure a receiver is appointed by the Comptroller. All moneys are paid into the United States Treasury, and dividends paid by the Comptroller. This method has proven very economical and expeditious in comparison with the system of appointing receivers by the courts, which prevails in several States.

I have briefly noted the distinguishing features of the national system. The National Bank Act has stood as a legislative model for the various States, and several have copied its provisions. But there is nothing approximating uniformity in the different States. The greatest diversity exists. Few States require banks of discount and deposit to keep a reserve or limit the amount of loans to single individuals, corporations, or firms, or forbid loans upon real estate, or stock of the bank, or forbid over-certification, or make stockholders liable to assessment for the payment of cred-

itors. Many have no system of examinations, many require less frequent reports of condition—quarterly or semi-annually—and less complete in form and detail than in the national system.

Some States have excellent systems, like New York. Kansas has a very complete law, recently enacted. In thirteen States State banks are prohibited from issuing circulating notes. In fifteen the statute is silent upon the subject. Many require securities, ranging from U. S. bonds to real estate, as a basis for circulation, and some permit circulation, without security, to an amount exceeding the capital stock. In one, an individual, by complying with the statute, becomes an "Individual Banker," possessing all the powers of a corporate bank, including that of issuing circulating notes. Trust companies form an important part of State banking institutions, enjoy unusual privileges, and have had marvellous growth in our cities. The city of Boston has no State banks, but many trust companies. New York's and Philadelphia's trust companies far surpass their State banks in volume of business and aggregate of resources. They are not allowed to issue circulating notes, and are not authorized to "discount bills," but may loan upon them or buy them. They exercise all the other usual functions of banks, and, in addition, may act as register and transfer agents for corporations, fiscal agents for municipalities; may accept and execute any trust of any kind, created by a corporation or individual, or by order of court. They pay interest upon deposits subject to check, and are strong competitors of savings' banks, as well as banks of discount. They are not required to keep reserve, and many of them keep no cash, but deposit with and pay by check upon their clearing-house bank.

In New York, savings banks can only invest in United States bonds, New York State bonds, municipal bonds within the State of New York, and bonds and mortgages. In all other States the range is much wider, including railroad and corporation bonds, and, in many, bills receivable. Most savings banks are mutual, but many have capital stock, and many do a commercial bank business.

The banking laws and systems of the several States are so different that comparison between the National and State systems is exceedingly difficult. Their relative importance is tersely expressed by the following table.

Total resources,	3,788 National banks, October 31, 1892	$3,510,094,897
" "	3,191 State banks, July 1, 1892	1,040,697,731
" "	168 Loan and Trust companies, July 1, 1892	600,244,908
" "	1,059 Savings banks, July 1, 1892	1,964,044,861
" "	1,161 Private banks, July 1, 1892	146,661,673

The currency question at the present time presents a triangular aspect. The government has in circulation five different kinds of paper money—gold certificates, silver certificates, greenback certificates, greenback and treasury notes—aggregating $899,562,711. The national banks have in circulation $174,404,-424, and now comes the proposition, formidable from the indorsement it has received, to restore circulation to State banks. Since 1878 the silver interests have dominated the councils of the nation. Under the Bland act silver was purchased, and $378,166,793 standard dollars coined. They accumulated in the Treasury, where their uselessness would doubtless have compelled the repeal of the act had they not been coaxed into circulation by means of a paper proxy—silver certificates.

In 1890, when the high rate of interest which prevailed in the money centres of the world indicated a scarcity of money and justified an increase in the circulating medium, a proposition was made to allow national banks to issue circulation to the par of their bond deposits. This proposition was absolutely free from criticism, and would have added (July 14, 1890) $14,412,190 to the circulation, almost immediately. And yet this silver interest barred the way and insisted that no relief should come except it came through silver. Free coinage was the panacea demanded; compromise gave us the present law, under whose provisions 129,-879,444 ounces of silver have been purchased and $124,735,665 Treasury notes issued. This silver has depreciated upon the hands of the Government $14,987,545. That is the bounty paid to the silver industry.

According to the late Mr. Blaine the "tariff is enlightened selfishness." If enlightenment is in proportion to selfishness, then silver advocates stand preëminent.

The silver industry is entitled to no bounty. The policy of the Government, in purchasing a commodity which it does not want, for the sole purpose of putting into circulation as money the obligations given therefor, cannot be justified. An equally safe and more elastic currency can be otherwise provided.

The operations of the act of 1890 have involved the Government in demonstrable loss and threaten to involve financial dis-

aster. The possibility of a premium upon gold, and consequent contraction of the currency by the amount of gold in circulation, holds enterprise in fetters, embarrasses trade and depreciates our securities in the markets of the world. The monometallists this country needs to fear are those who contemplate this prospect with equanimity, who would make merchandise of gold and make silver our basis of value. There is not a business interest that would not be relieved, not an industry that would not be strengthened, if the Government would cease these silver purchases and cease to issue currency.

The cloud that obscures the sunshine of prosperity has a silver substance, instead of a silver lining. National bank currency is flippantly condemned upon the ground that it is based upon the national debt, which is about to be extinguished, and hence the currency must cease to exist. This position is based upon three assumptions, by no means warranted: First, that no currency can be secure except it be based upon a deposit of stocks and bonds; second, that the United States debt will presently cease to exist; third, that when the national debt is paid and cancelled no other securities will exist available for the purpose.

If the banking experience of the several States prior to the war affords no example of a successful currency system, it nevertheless furnishes data sufficient to show what might have been. From this experience the national banking system was evolved. The practicability of the safety fund principle, when confined in its application to circulating notes and the issue of such notes sufficiently guarded, was fairly demonstrated. The perfect statistical information furnished by the national bank system more clearly demonstrates the feasibility of protecting bill-holders without bonds as security, if that alternative becomes necessary.

Since the organization of the national bank system, and prior to November 1, 1892, 181 banks have failed. All of these paid noteholders in full out of the proceeds of the United States bonds deposited to secure the same; 39 paid creditors in full; 6 paid principal and part of the interest, and 13 principal but no interest; 110 have been finally closed, and 16 are virtually closed. Of those finally closed, only 33 failed to pay dividends to creditors, equal in amount to their circulation, in addition to redeeming their notes.

The total circulation of these 33 banks was $3,310,529, their total dividends were $2,095,678. The total circulation of all these

failed banks was $16,840,850. The total cost to the government, from all sources, of the national bank system has been $14,535,000. The total tax collected from the banks, upon circulation alone, being at the rate of one per cent. per annum, was, June 30, 1892, $72,635,000. Hence from this tax alone the government could have assumed and redeemed all bills of all failed national banks, recouped all expenses and still have a net surplus of $41,209,150. An annual tax of two-fifths of one per cent., upon circulation would have defrayed all cost, and redeemed all notes of all failed banks.

In the light of the foregoing statistics it is probable that most banks would, without bonds as security, pay enough to redeem their circulating notes. Hence the Government, fortifying itself by means of a small tax, could safely assume the immediate redemption of the notes of failed banks, and by making itself a preferred creditor, recoup itself from the bank's assets.

But a safety fund which compels the strong banks to redeem the notes of the weaker ones is essentially unjust. The safety fund principle can be combined with security for circulation with excellent results. Let a fund be contributed by a uniform tax upon all banks, and paid into the Treasury of the United States, available for the immediate redemption of the notes of failed banks. Give this fund a prior lien upon the assets and stockholders' liability of such banks for the advances made, less the amounts contributed to such safety fund by such banks. There should be a provision, also, that any bank going into liquidation should only be required to deposit with the Treasurer of the United States a sum equal to its outstanding circulation, less the amount contributed by such bank to such fund. Such a fund would involve no injustice to banks, would be a guarantee of the immediate redemption of failed bank notes, and would avoid the criticism of the want of convertibility of other than United States bonds as a basis for circulation. The necessary legislation could be easily engrafted upon the present provisions of the National Bank Act.

As to the second assumption: public revenue, viewed in the light of public expenditures and the trend of public opinion upon the subject of taxation, affords no prospect of the reduction of the public debt by bond purchases in the immediate future. There is little probability of anticipating the maturity of the

four per cent. bonds, and every indication that they will be continued after they do mature—July 1, 1907.

As to the third assumption: When the best is removed, of necessity, the second best is promoted and becomes best.

United States bonds command the highest premium in proportion to interest paid, yield the lowest rate of interest to an investor, fluctuate least, are most readily convertible into cash, and from the point of safety are the best securities of the present time. But to assume that when they cease to exist the country will be bereft of securities possessing stability and convertibility, suitable as a basis for circulation, is unwarranted. With $559,589,200 of four per cent. bonds, with fourteen years to run, this question, What other bonds can be substituted? is not a burning one. Any change in the basis of circulation, whenever made, should be predicated upon the extinction or unavailability of these bonds. The needs of these banks enabled the Government (September 1, 1891) to continue $25,364,500 of four and one-half per cent. bonds at the low rate of two per cent., at the pleasure of the Government, while the four per cent. bonds netted an investor, at the same date, 2.7 per cent. Thus the banks in effect are contributing to the Government a saving in interest of seven-tenths of one per cent. annually upon $25,364,500, or $177,551.50.

It was demonstrated in the last annual report of the Comptroller of the Currency that had the 4 per cent. bond issue been refunded into 2 per cent. bonds on October 31, at current market value, it would have resulted in a saving to the Government of $67,161,551.47. A large portion of such bonds could undoubtedly be so exchanged. It is argued that this would increase the public debt. Certainly not. The accruing interest is as much a part of the debt as the principal. It would increase the principal, but in a greater degree reduce the interest and result in a large net saving. This would furnish ample bonds, selling at par, as a basis for circulation, and by allowing circulation equal to the par of bonds it would remove all force from the criticism that parties organizing new banks are compelled to tie up their capital by purchasing high-priced securities equal to one-fourth their capital stock.

No bank is required to own more than fifty thousand dollars in U. S. bonds, and, all expenses considered, circulation nets more than 6 per cent. Hence the above criticism has little

force, except as to small banks in new places, and little even then.

In order to keep their funds profitably employed banks are becoming large owners of investment securities. On December 9 they owned $153,648,180.71 of investment securities, in addition to $185,918,850 in U. S. bonds. The ownership of bonds is no hardship. It is the heavy tax and restricted issue and high premium that are unjust. Security for circulation compels the conservative investment of enough funds to absolutely protect bill-holders and leave the remaining assets for the protection of general creditors.

State bank circulation is advocated so as to give each locality an abundant supply of money. The profit of bank circulation depends upon the time it remains outstanding. It is useless to the public and profitless to the banks, so long as it remains in the bank vaults. As often as it is received and credited to a depositor, so often is it redeemed. Its use and profit are inconsistent with the ideal of a local currency.

In ante-bellum times banks uniformly discriminated in favor of the borrower, who wanted funds to use at a distance. State bank bills, if permitted to issue, must be accepted as money, must pass current with the business community, because the greater portion of the community are not in condition to discriminate between the strong and the weak, and of necessity cannot be; also because of competition—a fear that refusal may not be well founded and result in driving away business. Such bills would circulate freely in normal times, when credit is freely extended, would perform the function of money and pay debts; but in times of financial reverses, the general distrust that withholds credit would extend to them, and instead of being regarded as money, holders would be seeking their redemption; instead of paying debts, their own payment would be demanded. In times of prosperity they would add to the boom; in times of adversity they would lose their money power and add to the distress.

Why should Congress delegate the question of bank circulation to the forty-four sovereignties that constitute the United States, with diverse laws, systems, and supervision? Confusion, uncertainty, want of information and inability to procure information must ensue. It is axiomatic that one authority, with central supervision and control, can accomplish better re-

sults. You cannot localize money in the United States. The value of a currency depends upon the extent of country in which it possesses debt-paying power. Staté lines are all powerful in determining where a man shall vote and pay his taxes, but in determining the course of commerce and fixing the currency that moves that commerce, they should have no effect. The United States is a nation, in a commercial sense preëminently so, with one interest and one destiny, and its material interests will be best subserved by but one currency.

The greenbacks are a forced loan, bearing no interest, which must some day be paid. Our silver currency is non-elastic and certainly non-profitable. State-bank circulation is condemned alike by reason and experience.

The national-bank circulation is commended alike by reason and experience. Proper legislation could easily add elasticity to its present qualities and render it adequate to the needs of the entire country, making it what every currency should be—sound, safe, elastic, and as good as gold. And what stands in the way of such legislation—a prejudice as old as it is unjust, a selfishness that would force a market for silver, and a clamor for more money as unwise as it is dangerous.

Carefully prepared statistics, covering widely separated periods, show that over ninety per cent. of all business transactions in the United States, accomplished through banks, are represented by credits. Less than ten per cent. involves the actual transfer of money. In the light of this fact, how apparent becomes the impossibility of furnishing a volume of money, sufficient to transact the business of the country in times of distrust when credit is refused. The mechanism of banking is so complete and its working is so thoroughly systematized that some form of credit is made to take the place of money, wherever possible, thus avoiding the risk involved in the use of money and preventing the loss of interest which such money otherwise employed would earn. A check drawn upon the First National Bank of Potsdam and deposited in the First National Bank of Canton—two adjoining towns in northern New York—would be sent to New York City for collection, a distance of four hundred miles, instead of being sent direct, a distance of ten miles. Why ? Because there is no exchange between these towns, no open accounts. There is between each and New York. A

Michigan bank has occasion to remit to a bank in Missouri. It does not send money, which would involve express charges. It remits by draft upon New York, Chicago or some central city, where it has a credit balance, which costs only postage. Thus the bulk of all the banking transactions of the country flow into our larger cities, constitute a part of the Clearing-House exchanges, are subject to every possible offset, and the actual money remittances from one locality to another are minimized. The Clearing-House affords the most remarkable instance of the extent to which a simple device of bookkeeping can minimize the use of money.

In our smaller cities it is the custom of banks to send all claims payable at other banks in the same place, by runners or messengers to such banks for payment. In such manner are their exchanges consummated, and in such cases the payment of these claims represents a money transaction. In our larger cities, in order to save time and labor and avoid the risk attendant upon the transporting of money about the streets, and minimize the amount of actual money required to adjust the exchanges, clearing-house associations have been established, wherein each bank is credited with what claims it has against the other members of the association, and debited with the amount that each of the other members of the association hold against it. The balance only is paid or received in money. Thus each bank adjusts its day's exchanges, as though all transactions were with one bank instead of with the many banks which constitute the other members of the association. The mechanism is simple. The claims against each bank are placed in separate envelopes and listed on the outside. Each bank has a desk in the Clearing-House, and is represented by a delivery clerk and a settling clerk. The delivery clerk upon arrival hands to the Manager a ticket showing the total amount of exchange brought. This amount is immediately credited upon the Clearing-House balance sheet.

All clerks must be at their desk at ten o'clock. Any delinquent bank is fined. At the tap of the bell the procession of delivery clerks moves in order, each delivering his exchanges and each settling clerk receiving and receipting therefor. The settling clerk then foots the exchanges he has received from the other banks and sends to the manager a ticket, showing the amount. Each bank is debited the amount thus received and

the total credits and total debits balance. If they do not, after the expiration of fifteen minutes, the time allowed for the consummation of this work, any bank found in error is fined.

At 1:30 P. M. the banks are again represented at the Clearing-House, and either pay or receive in money their debit or credit balances. The payments just balance the receipts, and of all the millions that pass through the Clearing-House each day, nothing remains at the close of banking hours.

There are fifty-seven clearing-house cities in the United States. Their aggregate exchanges last year were $61,017,839,067 and yet the transaction of this enormous volume of business was accomplished with the use of $4,881,777,289 in money, such being the total balance actually paid.

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